Further, there is no legitimate public policy basis for requiring an incumbent LEC to subsidize competitors who are clearly capable of assuming the financial burdens associated with market entry and who, in some instances, have greater access to capital than the incumbent LECs themselves. Moreover, as documented below, the establishment of a regulatory structure that requires LECs to subsidize and support the operation of their competitors would be constitutionally infirm.

E. AT&T's Interpretations Of The Act Are Anti-Competitive Notice Section II.B.2., 3.

The single entity most likely to benefit from a non-compensatory interconnection regime is AT&T. AT&T has a huge national network, as well as the nation's largest cellular system. It has an already deployed system of switches with local exchange switching capability. And, its brand name recognition is so great that people associate the AT&T brand name with products the company does not even sell.[37] AT&T is also the primary proponent of rules which would favor itself, as an individual competitor, rather than competition.

If the Commission adopts pricing measures that require LECs to dedicate services and facilities to AT&T and other competitors below their economic costs (which is what AT&T advocates), AT&T could dominate the local and long distance markets, and suppress technological innovation and facilities-based competition,

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when the customer is controlled by an entity other than the incumbent LEC. See below.

[37] Harris and Yao Affidavit at 35-37.

eviscerating the intent of the 1996 Act. As the Harris and Yao Affidavit demonstrates, AT&T's advocacy, if embraced, could severely disrupt competition, investment, facilities-based competition and the nation's telecommunications infrastructure. Because the anti-competitive aspects of AT&T's advocacy might not be patent, some discussion is warranted.[38]

AT&T's positions are simply stated, despite their complex and significant consequences. First, AT&T contends that the 1996 Act grants it access to incumbent LEC services and facilities at huge discounts below the cost of providing the services or constructing the facilities. AT&T has announced that it is entitled to more than an 85% discount from the existing price of LEC-provided interstate access. In other words, AT&T asserts that it should pay less than 15% of existing access prices for local interconnection.[39]

AT&T disguises its demands by stating that it is entitled to purchase network elements at its own version of long-run incremental cost.[40] The Hatfield Study,[41] often relied on by AT&T, is an example of how questionable economics can be used to manipulate costs to disguise below-cost service. However, as AT&T itself

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[38] See id. at 30-35 for a discussion of the potential anti-competitive effects of AT&T's advocacy (as well as other IXCs) within the context of its market and business strategies.

[39] Obviously, the other two large IXCs would also benefit, to a lesser extent, from an anti-competitive set of interconnection rules. MCI, in fact, has joined with AT&T in demanding this outrageous discount.

[40] See attachment, "Interconnection, Unbundling and Total Service Resale" at 38-57, to AT&T letter to Regina Keeney, Chief, Common Carrier Bureau, dated March 21, 1996 (cited in the Notice at n.126).

[41] See Exhibit B at 4.

has repeatedly recognized, pricing a service at the level it has demanded for LEC services is economically unreasonable.[42]

Second, AT&T has demanded unbundled access to over 100 functions, facilities, data bases, and real estate, all to be priced below the cost of providing the service to AT&T.[43] Finally, AT&T has demanded that local exchange services be priced on a wholesale basis at a price which grants AT&T a discount of 28% off of existing U S WEST prices.[44]

The Harris and Yao Affidavit discusses at some length the danger of blithely accepting AT&T's advocacy or acceding to its interconnection demands. If AT&T's interpretation of the 1996 Act were accepted, it would result in the elimination of existing and potential competition to AT&T. For example, incumbent LECs could not compete because they would be required to offer below-cost services to AT&T. More important, AT&T's demands on the capital and other financial resources of the incumbent LECs, as well as their time, would make it impossible for the LECs to construct anything for their own customers, or to replace their plant when it

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[42] See Joint Brief of Petitioner AT&T Corp. et. al., California v. FCC, No. 94-70197, Ninth Cir., filed Aug. 17, 1995 ("prices for telecommunications services must exceed marginal costs (and make a contribution to fixed costs) for carriers to remain financially viable").

[43] See attachment to AT&T letter, supra. n.40, at 8-37 ("Unbundled Access to Network Elements") for a description of some of the network elements for which AT&T seeks unbundled access.

[44] See Public Utilities Commission of the State of California, Decision 96-03-020, Mar. 13, 1996 at 10-13.

became obsolete or dysfunctional. LEC resources would be consumed by constructing facilities for, and serving the business purposes of, AT&T.

Of equal significance, adoption of the AT&T position would retard new entry and potentially drive other entrants out of the market. Because AT&T would be in a position to underprice new entrants on the backs of the resources of the incumbent LECs, recent or new entry would become increasingly difficult to accomplish or sustain. The establishment of below-cost interconnection, network elements, and resale, the main drivers in AT&T's strategy, would make it uneconomical for other competitors to construct their own facilities.

AT&T already has huge brand recognition advantages, massive existing cellular and interexchange networks, and an existing array of switches capable of providing local exchange service. Allowing AT&T to underprice facilities-based competition, by reselling below-cost incumbent LEC services, would enable AT&T to substantially delay implementation of its own network construction plans until a competitor developed new technologies which were not only superior to (and less expensive than) existing technology, but also superior to the existing technology, minus the wholesale discount. Until such dramatic new technology was developed, AT&T could dominate the local exchange market without ever building its own facilities, thus inefficiently hindering investment and technological progress in local exchange telephony.[45]

[45] See Harris and Yao Affidavit at 23-26, 29-30, 32-35.

Indeed, solely through its resale strategy, AT&T could selectively recreate the old Bell System. It would, of course, reassemble only the lucrative portion of that System, leaving the remaining high-cost/low-revenue segment of the industry as a burden to be dealt with by the LECs and by society in general. It will have, quite conveniently, avoided the burdensome regulatory constraints and obligations which had historically governed the Bell System operations.[46]

The ultimate irony of AT&T's position is that it takes a pro-competitive statute, like the 1996 Act, and construes it to accomplish -- as to itself -- the virtual elimination of meaningful market competition. It would be arbitrary and unlawful to enact regulations which permitted or encouraged such a result.

F. The Commission Must Recognize Constitutionally Protected Property Interests Notice Section II.B.2.

In promulgating regulations that implement the 1996 Act, the Commission must avoid an interpretation of Section 251 that renders the 1996 Act unconstitutional. It has long been an axiom of statutory interpretation that statutes must be interpreted to avoid serious constitutional problems.[47] The roots of this well-established principle of statutory interpretation lie in Chief Justice

[46] AT&T's demand on incumbent LECs also constitutes a transparent attempt to delay BOC entry into the interLATA business by retarding the development of facilities-based competition. See discussion below.

[47] Public Citizen v. U.S. Dept. of Justice, 491 U.S. 440, 466 (1989); Communications Workers of America v. Beck, 487 U.S. 735, 762 (1988) ("[F]ederal statutes are to be construed so as to avoid serious doubts as to their constitutionality[.]").

Marshall's opinion in Murray v. Schooner Charming Betsy.[48] From Marshall's words evolved "[t]he elementary rule . . . that every reasonable construction must be resorted to in order to save a statute from unconstitutionality."[49]

This approach not only reflects the prudential concern that constitutional issues not be needlessly confronted, but also recognizes that Congress, like the courts, is bound to uphold the Constitution.[50] The courts "will therefore not lightly assume that Congress intended to infringe constitutionally protected liberties or usurp power constitutionally forbidden it."[51]

This cannon of statutory interpretation extends to regulations implementing statutes. Unless the construction is plainly contrary to the intent of Congress, statutes must be interpreted so as to defeat administrative regulations that raise substantial constitutional questions.[52]

1. Ratemaking
Notice Section II.B.2.

Some interested parties contend that pricing for interconnection and unbundled elements under Section 251 should be based upon cost principles that do

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[48] 6 U.S. (2 Cranch) 64, 118 (1804) ("[A]n act of Congress ought never to be construed to violate the law of nations if any other possible construction remains[.]").

[49] Hooper v. People of State of California, 155 U.S. 648, 657 (1895).

[50] DeBartolo Corp. v. Fla. Gulf Coast Bldg. & Const., 485 U.S. 568, 575 (1988).

[51] Id. See also Grenada Co. v. Brown, 112 U.S. 261, 269 (1884).

[52] Bell Atlantic Telephone Companies. v. FCC, 24 F.3d 1441, 1445 (D.C. Cir. 1994).

not permit a reasonable contribution to the overall operation and investment of the LECs. The most extreme example is AT&T's often publicly repeated assertion that it is entitled to prices based on costing principles that grant it a more than 85% discount on access charges. Other versions of cost methodology set forth by potential interconnectors reach a similar, albeit less extreme, result.[53]

Required use of such a cost methodology would result in a confiscation of the property of incumbent LECs in violation of the Fifth Amendment to the United States Constitution. Nothing in the 1996 Act suggests that Congress intended such a result. Where there is no express authorization in an act of Congress for an agency to take private property, an effective taking is unlawful because it usurps Congress' legislative and appropriation powers.[54] And, where there is taking authority, Congress would still need to provide for compensation to the private party whose property was taken. Within that compensation obligation, there would be no room for confiscatory ratemaking.

The Takings Clause of the Fifth Amendment commands that private property shall not be taken for public use without just compensation.[55] The guiding principle of the Takings Clause is that some property holders should not be singled out to

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[53] See, e.g., "Implementing Local Competition Under the Telecommunications Act of 1996, A Proposed Handbook for the FCC," prepared by ALTS, updated Apr. 8, 1996, at 9 n.7, 16, 21 ("ALTS Handbook").

[54] Ramirez de Arellano v. Weinberger, 745 F.2d 1500, 1510 (D.C. Cir. 1984) (en banc), vacated on other grounds, 471 U.S. 1113 (1985).

[55] U.S. Const. Amend. V, cl. 4.

bear burdens that, in all fairness, should be borne by the public as a whole.[56] Accordingly, while competition in the local telephone market is a beneficial legislative goal, incumbent LECs cannot, consistent with the Fifth Amendment, be required to shoulder the entire burden of bringing competition to that market.

Although common carriers are regulated entities that devote their property to public use, the Supreme Court has long recognized that a carrier's property remains private property and is entitled to the same protection from unlawful takings as any other property.[57] Courts continue to hold that even in this era of pervasive government regulation, the Takings Clause protects public utility property from unlawful government action.[58]

In the context of utility rate regulation, the Fifth Amendment protects utilities from being compelled to charge rates that are so unjust as to amount to a confiscation of their property. "If a rate does not afford sufficient compensation, the [government] has taken the use of utility property without paying compensation."[59] Thus, to avoid a confiscation of their property, public utilities -- LECs included -- are entitled to charge a rate that is both just and reasonable.

The Supreme Court has determined the criteria of a rate that is "just and reasonable" for the provision of service to the public. In Federal Power Com'n v.

[56] Armstrong v. United States, 364 U.S. 40, 49 (1960).

[57] Western U. Teleg. Co. v. Pennsylvania R. Co., 195 U.S. 540, 569 (1904).

[58] Colorado Springs Prod. Assoc. v. Farm Credit Admin., 967 F.2d 648, 655 n.8 (D.C. Cir. 1992).

[59] Duquesne Light Co. v. Barasch, 488 U.S. 299, 308 (1989).

Hope Natural Gas Co.,[60] the Court held that determination of a just and reasonable rate involves a balancing of investor and consumer interests. The Hope Court recognized that utility investors have "a legitimate concern with the financial integrity of the company whose rates are being regulated."[61] In accordance with this recognized interest, the Court held that a just and reasonable rate permits a utility to earn enough revenue to cover not only its full operating expenses, but also the capital costs of doing business.

The return to investors, or profits, should be commensurate with returns on investments in other industries having corresponding risks.[62] As one of its reasonable expenses of providing service to the public, a utility is entitled to recover its depreciation expenses.[63] Regarding capital costs, a utility should recover its service on its debt and pay dividends on its stock.[64] In short, a just and reasonable rate enables a utility to operate successfully, maintain its financial integrity, attract capital, and compensate its investors for the risks they have assumed.[65]

Pursuant to this constitutional mandate, the Commission must ensure promulgation of rates for interconnection and unbundling that permit incumbent

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[60] 320 U.S. 591, 603 (1944).

[61] Id.

[62] Id. And see Bluefield Waterworks & I. Co. v. Public Service Com'n, 262 U.S. 679, 692 (1923).

[63] Louisiana Public Service Comm'n v. FCC, 476 U.S. 355, 364-65 (1986).

[64] Hope Natural Gas, 320 U.S. at 603. Regulatory actions which coerce a negative cash flow (e.g., U S WEST was forced to sustain a negative cash flow in 1995) make a company more vulnerable to industry consolidation.

[65] Hope Natural Gas, 320 U.S. at 605.

LECs to recover their full costs of providing interconnection and unbundled network elements as well as a reasonable profit. Any other interpretation would amount to a confiscation of utility property that would render the 1996 Act unconstitutional. Indeed, courts have already held that requiring a telephone company to provide interconnection to its competitors without adequate compensation is a taking in violation of the Fifth Amendment.[66]

Moreover, in the context of this docket, the Commission cannot establish a rate for interconnection on the assumption that rates for other services will compensate LECs for the loss. Under both the 1996 Act and the Commission's proposed rules, interconnection is intended to permit competitors to access LEC customers. If interconnection prices are set below actual cost, competitors will be given an unfair (and unlawful) advantage over LECs in competing for the LECs' own customers. Given the significance of the potential damage to the LECs from such a situation, one regulator cannot assume that another regulator will make up for the harm caused by below-cost pricing by increasing other rates. Nor can a regulator ignore the impact of below-cost pricing by hoping that other prices controlled by that regulator might be set so as to recapture the actual cost of operating the business.

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[66] See State ex rel. Public Service Comm'n v. Skagit River Tel. & Tel. Co., 85 Wash. 29, 45, 147 P. 885 (1915), modified on other grounds, 89 Wash. 625, 155 P. 144 (1916); Pacific Tel. & Tel. Co. v. Eshleman, 166 Cal. 640, 665-87, 137 P. 1119 (1913).

Shifting to the LEC retail services costs properly attributable to interconnection would simply exacerbate the harm caused by below-cost pricing, by driving retail customers to the LEC's competitors. Such action clearly would not heal what would otherwise be a mortal constitutional wound.

2. Physical Takings
Notice Section II.B.2.

The need to create regulations that protect incumbent LEC property interests is even more important because the 1996 Act authorizes and, with respect to unbundling, requires physical per se takings of LEC property.[67] The 1996 Act also requires incumbent LECs to provide competitors the unbundled network elements themselves, e.g., loops, switches. These network elements are tangible, physical property taken by the government from one competitor and given to another competitor.

All of the above requirements involve physical occupations of incumbent LEC property. As such, they amount to per se takings under the Fifth Amendment.

In the seminal decision of Loretto v. TelePrompTer Manhattan CATV Corp.,[68] the Supreme Court held that a permanent physical invasion of property is such an unusually serious governmental intrusion that it is a taking of property per se under the Fifth Amendment. Thus, if the governmental action involves a physical

[67] Section 251(c)(6) of the 1996 Act requires incumbent LECs to allow physical or virtual collocation of competitor equipment, as necessary for interconnection and to access unbundled network elements.

[68] 458 U.S. 419 (1982).

occupation of property, the government's policy objectives in permitting the occupation are irrelevant.[69] Even when the economic impact on the property owner is minimal, a physical occupation is a compensable taking.[70]

The Supreme Court has zealously guarded property owners from physical takings because, when the government sanctions a physical occupation of any kind, it denies the property owner the right to exclude others. Traditionally, this right has been considered "one of the most treasured strands in an owner's bundle of property rights."[71] When the government compels a physical invasion of property "the government does not simply take a 'strand' from the 'bundle' of property rights: it chops through the bundle, taking a slice of every strand."[72] Because physical collocation requires LECs to permit permanent physical occupations of their property, two courts have already held that physical collocation constitutes a per se taking of incumbent LEC property.[73]

Virtual collocation, as typified by the Commission's extant virtual collocation rules,[74] so divorces the LEC "owner" of the virtually collocated equipment from all

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[69] Id. at 434.

[70] Id.

[71] Id. at 435-36; Kaiser Aetna v. United States, 444 U.S. 164, 179-80 (1979).

[72] Loretto, 458 U.S. at 435.

[73] Bell Atlantic, 24 F.3d at 1445 (finding no statutory authority allowing the Commission to take private property, but not explicitly finding a taking); GTE Northwest, Inc. v. Public Utility Comm'n of Oregon, 900 P.2d 495, 503-05 (Ore. 1995).

[74] See 47 CFR §§ 64.1401, 69.121.

legal indicia of ownership that it results in precisely the same taking of property as physical collocation.[75]

Loop unbundling is, in many senses, even more intrusive than physical collocation (including the virtual variation). At least in the case of physical collocation, some of the LEC's property remains available for the LEC to use. In the case of dedication of an unbundled loop to a competitor, all LEC control over its property -- the loop -- is lost.

The fact that the occupation of unbundled loops, in the physical sense, may be short in duration and intermittent does not diminish the taking aspect of the conduct in that situation where competitors are granted a permanent right to use the loops. As the Supreme Court recognized in Nollan v. California Coastal Com'n,[76] a permanent physical occupation occurs "where individuals are given a permanent and continuous right to pass to and fro, so that the real property may continuously be traversed, even though no particular individual is permitted to station himself permanently upon the premises."

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[75] The Notice concludes that the Commission's virtual collocation rules should remain in place for both tariffed virtual collocation and Section 251 interconnection "in light of the Court decision in *Pacific Bell v. FCC* . . . ." Notice at ¶ 73 (footnote omitted). In Pacific Bell, various incumbent LECs challenged the Commission's virtual collocation rules as an unauthorized taking of property. The Court remanded the case because the 1996 Act specifically authorized virtual (as well as physical) collocation. See Judgment, Pacific Bell v. FCC, No. 94-1547 (D.C. Cir. Mar. 22, 1996). The Constitutional issues raised in Pacific Bell were not resolved in favor of the Commission. Rather, they remain very much alive and are reasserted here.

[76] 483 U.S. 825, 831-32 (1987).

The Supreme Court in Loretto stated that a property owner suffers "a special kind of injury when a stranger directly invades and occupies the owner's property."[77] That "special injury" is even more pronounced when the invasion is by a competitor. To require incumbent LECs to permit their competitors "to exercise complete dominion" over the LECs' property -- even if intermittently -- "literally adds insult to injury."[78]

The fact that the 1996 Act now expressly authorizes collocation and mandates unbundling neither diminishes the governmental taking nor invalidates those decisions holding that collocation is a physical taking. Rather, the Fifth Amendment requires the government to provide incumbent LECs with just compensation for the occupation of their property. Just compensation requires the realization of the full market value of the property taken. Where rules which result in takings of property, affected LECs must be permitted either to recover: a) the full value of the taken property from the interconnector; or b) this value from the interconnector and the sovereign.

3. Construction Of Facilities Notice Section II.B.2.

Both the 1996 Act and the Notice presume incumbent LECs will construct facilities under regulatory compulsion, in at least two instances: 1) construction associated with the unbundling of facilities to permit interconnection and network

[77] 458 U.S. at 436.

[78] Id.

element selection; and 2) construction of new facilities for competitors at their request. However, the issue of when, and whether, a LEC can be required by the government to construct facilities also has constitutional implications. These implications are even more grave when the mandated construction is for a competitor.

Historically, the duty of carriers to construct has been assumed. However, the Commission's rules have always ensured that each LEC has the "opportunity to earn a rate of return 'commensurate with returns on investments in other enterprises having corresponding risks' and 'sufficient to assure confidence in the financial integrity of the enterprise,' as to maintain its credit and to attract capital."[79] Thus, forced construction by LECs was not at their risk.

In a competitive marketplace, U S WEST perceives that any regulatory guaranty of its ability to be profitable will no longer be meaningful, as a general principle. Nevertheless, the Commission cannot adopt rules which deprive an incumbent LEC of this reasonable opportunity. Moreover, the Commission cannot coerce an incumbent LEC to construct facilities without ensuring that the cost of such involuntary construction is fully recovered.

Simply stated, the Commission cannot require incumbent LECs to assume the costs of unbundling network elements or constructing new facilities for their competitors without having effectuated a taking of LEC property. When a statute

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[79] In the Matter of Amendment of Parts 65 and 69 of the Commission's Rules to Reform the Interstate Rate of Return Represcription and Enforcement Processes, Report and Order, 10 FCC Rcd. 6788, 6824 ¶ 76 (citation omitted).

compels a property owner to construct a facility for public use without compensation, the sovereign has taken property in violation of the Takings Clause.[80]

If the Commission requires incumbent LECs to assume the costs of unbundling network elements and/or constructing facilities for competitors or others, the taking is even more dramatic than a permanent physical occupation. Certainly, if the Supreme Court held that a taking occurred when New York required Ms. Loretto to suffer a cable installation on her apartment building, it would hold that an even greater infringement of her property rights occurred if she was also required to pay for the installation of the facilities herself. The Commission cannot require incumbent LECs to suffer permanent physical invasions of their property through allowing competitors access to their unbundled loops and concomitantly require incumbent LECs to pay for the privilege of the taking.

The goal of a competitive local exchange telephone market does not justify a taking of incumbent LEC property. A requirement that LECs construct facilities for the use of others is no less a taking -- indeed, it is more so -- when the requirement

[80] See, e.g., State of Washington ex rel. Oregon R.R. v. Fairchild, 224 U.S. 510 (1912) (state railroad commission's mandate that railroad construct track connections between competing railroads at its own expense for purpose of facilitating the interchange of business constituted a taking of property); Great Northern Ry. Co. v. Minnesota, 238 U.S. 340 (1915) (requiring railway to erect scales in a village stockyard constituted a taking of property); see also ICC v. Oregon-Washington R.R. & Navigation Co., 288 U.S. 14 (1932) ("[T]o require extension of existing lines beyond the scope of the carrier's commitment to the public . . . is a taking of property in violation of the Federal Constitution"); and Midwest Video Corp. v. FCC, 571 F.2d 1025, 1058 (8th Cir. 1975) (opining that proposed regulation requiring cable companies to construct facilities and dedicate them to public use without compensation would be a taking in violation of the Fifth Amendment).

benefits competitors.[81] Accordingly, to ensure that the property of incumbent LECs is not taken in violation of the Fifth Amendment, the Commission must ensure that incumbent LECs are compensated fully for unbundling network elements and receive fair market value for the construction of facilities.

Any construction requirements imposed by the Commission must include a component for ensuring cost recovery of that construction. In the context of this rulemaking, the Commission must establish a framework whereby costs incurred in unbundling LEC networks for the purpose of providing interconnection or network elements can reasonably be recovered on a timely basis.

4. Equal Protection
   Notice Section II.B.2.

Were the Commission to resolve upon a structure which favored individual competitors rather than competition, an entirely new set of constitutional difficulties would be raised, i.e., specifically, potential violations of the Equal Protection Clause of the Fifth Amendment. The requirement that any adopted Commission rules look toward protecting competition, not individual competitors, assumes constitutional significance because the Commission's rules contemplate

[81] See, State of Washington ex rel. Oregon R.R., supra; Pacific Tel. & Tel. Co. v. Eshleman, 166 Cal. at 687, 700-01. In addition to such a regulatory mandate constituting a taking, it is simply unfair to require LECs to capitalize competitive entry in light of the obvious financial resources of those demanding LEC construction on their behalf. Compare Order Adopting Rules and Renoticing Rules, Docket No. RMU-95-5, Iowa Department of Commerce Utilities Board, Apr. 5, 1996, at 8, wherein the Board notes that its "unbundling rules do not contemplate compelling a local utility to construct facilities for another local utility."

utilizing the property of incumbent LECs as the vehicle for promoting competition. Stated simply, U S WEST lawfully may not be compelled to dedicate its own private property to advance the private interests of interconnectors. U S WEST cannot be required to subsidize or underwrite any private company, even in the holy name of "competition."

In the past, legislation and regulations touching economic matters often received perfunctory consideration under the Equal Protection Clause. However, in recent years, courts have recognized that the fundamental societal value of equality should not lose its vitality when economic legislation is at issue.[82] As the Supreme Court noted in Dolan v. City of Tigard,[83] "simply denominating a governmental measure as a 'business regulation' does not immunize it from constitutional challenge on the grounds that it violates a provision of the Bill of Rights. . ."

The fact that legislation is intended to further the cause of competition in a particular industry does not insulate it from challenge under the Equal Protection Clause. In Metropolitan Life Ins. Co. v. Ward,[84] the Supreme Court struck down a state statute designed to give tax credit to domestic insurance companies in order to assist those companies competing with foreign insurance companies, holding that the statute violated the Equal Protection Clause. The Court held that while bringing in new businesses is a legitimate legislative goal, promoting those

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[82] Long Island Lighting Co. v. Cuomo, 666 F. Supp. 370, 418 (N.D.N.Y. 1987), vacated in part, on other grounds, 888 F.2d 230 (2d Cir. 1989).

[83] 114 S. Ct. 2309, 2320 (1994).

[84] 470 U.S. 869 (1985).

businesses by discriminating against would-be competitors is not a legitimate legislative goal.[85]

As the Court recognized, if promotion of a particular business or businesses were always a legitimate legislative purpose, the Equal Protection Clause would cease to have any force. Were such the case, a state or federal government could impose any discriminatory measure it desired so long as the legislator could show that the statute was intended to benefit the preferred business or businesses.[86]

Thus, while the Commission can, and should, develop rules that foster competition in the local telephone market, it cannot do so by discriminating against incumbent LECs. This is especially true if incumbent LECs are required to subsidize their competitors; and, even more so, if they are required to subsidize a particular group of such competitors in a manner which actually thwarts competition.

5. Essential Legal Premises
Notice Section II.B.

Based on the foregoing, several significant legal and constitutional premises must guide the Commission's analysis and implementation of the interconnection portions of the Act:

- Interconnection prices must be set at a level which is consistent with operating the entire LEC business at a profit.

[85] Id. at 880.

[86] Id. at 882.

- Provisions of the 1996 Act which constitute physical takings must be treated as such, and rates must reflect the LEC's constitutional right to just compensation.

- Mandated construction obligations are neither good policy nor legally free of consequences. Such mandates constitute a constitutional taking and rules must permit a LEC a guaranty of recovery of costs incurred in such construction.

- Rules which skew market forces by favoring a specific set of competitors, rather than competition, violate the Constitution's guaranty of equal protection under the law.

II. GOOD FAITH NEGOTIATIONS
Notice Section II.B.1

The key to the reasonable development of interconnection under the 1996 Act is good faith negotiations. The mark of good faith negotiations is when all parties to a negotiation pursue their own interests with the ultimate goal of finding a mutually satisfactory position that leaves all parties better off than if no agreement had been reached. An element of good faith negotiation is the willingness of a party to actually negotiate interconnection on a good-faith business basis. Good faith does not exist in the abstract, but in a business setting between two business operations.

The Commission's discussion of good faith negotiations in the Notice carries with it the disturbing suggestion that certain incumbent LEC practices fall into the category of "bad faith" tendencies. Clearly, good faith negotiation would not be undertaken if a party had no intention of entering into any agreement,[87] but a negotiating party's pursuit of its best interests in a negotiation can hardly be deemed "bad faith." Because U S WEST disagrees with certain of the Commission's implications in its discussion of good-faith negotiations, it here address several negotiation issues.

A. Confidentiality
Notice Section II.B.1.

The Notice implies that a party to an interconnection negotiation would not be negotiating in good faith if it were to require the other party to enter into a confidentiality agreement.[88] The Commission's suggestion merits brief attention.

U S WEST anticipates that any interconnection negotiation session may well involve mutual review of confidential business information of the parties. For example, one party's cost information, business plans, or other deployment information might need to be shared during negotiations. Moreover, a party to a negotiation could legitimately desire to keep a particular offer, or negotiating position, confidential, at least until such offer or position had been accepted.

Maintaining the confidentiality of negotiations is standard practice in the business world; and, by incorporating a right to confidentiality,[89] the 1996 Act

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[87] The Notice cites Southern Pacific Com. Co. v. AT&T, 556 F. Supp. 825 (D.D.C. 1983) as an example of "bad faith" negotiation. See Notice ¶ 47 & n.61. That case did not find any bad faith negotiation.

[88] Notice ¶ 47.

[89] See 1996 Act, 110 Stat. at 66, 68-69 (§§ 252(a),(e)) and compare 1996 Act, 110 Stat. at 70 (§ 252(h)). See also 1996 Act, 100 Stat. at 148 (§ 222(a)-(b)).

sanctions this practice. Accordingly, parties to interconnection negotiations have a legitimate right to demand that confidential information will be maintained in confidence, subject to a rigidly enforceable confidentiality agreement, and that the negotiations themselves will be confidential. There is nothing inherently bad, illegitimate or inappropriate in either party making such a demand.

The Commission's suggestion that a party demanding a confidentiality agreement be executed prior to commencing interconnection negotiation is acting in bad faith is wrong. The suggestion finds support neither in the 1996 Act nor in commonplace reasonable business expectations or practices.

B. Plans And Commitments
Notice Section II.B.1.

What does find support in commonplace reasonable business expectations and practices is that a negotiation involve reasonable demands, demands capable of being fulfilled by a party to the negotiation. An element of good faith negotiation certainly includes that a company seeking interconnection disclose what it wants to buy, where, when and for what duration.[90] LECs should be permitted to demand specific commitments in these areas as part of the interconnection negotiations.[91]

By the same token, it is bad faith for an interconnector to demand that a LEC unbundle its network elements immediately, expending substantial resources in the process, while refusing to provide the LEC with a schedule of anticipated purchase and deployment. It is possible that a competitor will demand that an incumbent LEC unbundle its entire network yet without any intent to purchase the unbundled elements in the foreseeable future, requiring the LEC to expend significant resources. This possibility is not speculative. Certain interconnectors would have the incentive to engage in this conduct.

The completion of "good faith" negotiations are a Checklist requirement.[92] The LECs should not have Checklist compliance held hostage by what, on its face, is clearly not the initiation of good faith business negotiations.

No potential interconnector should have the ability to initiate a broad, open-ended interconnection wish list, and later claim that failure to accommodate the

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[90] AT&T, for example, simply refuses to provide any specificity as to what it wants by way of interconnection facilities or services. It simply proclaims, as a matter of right, to be able to demand immediate availability of a wide array of interconnection points and network elements, without any type of commitment (or even information) as to whether it will purchase any of these facilities or services if they are made available in any particular location. In sharp contrast to AT&T's unreasonable position, potential facilities-based interconnectors have approached U S WEST with specific interconnection proposals.

[91] There is no current recovery mechanism for interconnection facilities constructed (or unbundled) under the circumstances.

[92] See 1996 Act, 110 Stat. at 62 (§ 251(c)), 88 (§ 271(c)(2)(B)).

overreaching demands deprives it of the ability to become facilities based. Such a bargaining position is predictable, particularly as it would have the effect of precluding a LEC's application to the Commission for interLATA relief. Incumbent LECs should have the right to require certain minimum "good faith" conduct with respect to "good faith" negotiations. That conduct should include, at a minimum, an obligation that a potential interconnector disclose and commit to certain points of interconnection and purchase commitments at identified locations within a reasonable purchase time frame.

III. COST PLUS REASONABLE PROFIT Notice Section II.B.2.

The Notice seeks comment on how the "cost plus reasonable profit" statutory language for pricing network elements should best be interpreted.[93] The appended Harris and Yao Affidavit addresses this issue at length.[94] Network elements priced too low could disrupt services of incumbent LECs, reduce their incentives to invest, and make investment by competitors unlikely and imprudent. Network elements priced too high could tend to drive uneconomic facilities construction and could delay competition.

U S WEST submits that network element costs are reasonable if they are based upon a costing methodology which, if applied to all U S WEST services, would

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[93] Notice ¶¶ 121, 129, 131. Other costing principles are discussed below -- wholesale pricing and "additional costs of termination.

[94] See Harris and Yao Affidavit at 5, 17-22.

result in U S WEST covering its total expenses and investment plus a reasonable profit. The Harris and Yao Affidavit describes proper application of a TSLRIC analysis and how such an analysis fits into pricing under the Act.

Within these general parameters, reasonable negotiating positions ought to be relatively simple, with one additional Commission guideline. In this proceeding, the Commission should clearly and forcefully dispel the notion that the 1996 Act somehow compels incumbent LECs to provide interconnection services at prices which would not permit LECs to cover their operating costs and investment. No reasonable corporation would invest in new facilities under these circumstances, or repair or upgrade existing facilities. In fact, no reasonable corporation would do business under such circumstances.

Such pricing would be anti-competitive and would favor only those few corporations with huge embedded networks, switching capacity, brand name recognition, and freedom from any pricing rules.[95] The Commission should make clear that no one is entitled under the Act to services or facilities priced below the level described herein.

IV. POINTS OF INTERCONNECTION
Notice Sections II.B.2.

The Act and the Notice call for comment on two different types of "unbundling": 1) interconnection must be provided at any "technically feasible

[95] See id. at 6, 7, 10-14, 22-26, 29-35.